IN THE

Supreme Court of the United States

OCTOBER TERM, 1975

No. 75-602

CABOT CORPORATION, *Appellant,*

v.

PUBLIC SERVICE COMMISSION OF WEST VIRGINIA and TRUE TEMPER CORPORATION, *Appellees.*

On Appeal from the West Virginia Supreme Court of Appeals

JURISDICTIONAL STATEMENT

F. PAUL CHAMBERS
MICHAEL A. ALBERT
1601 Kanawha Valley Building
Charleston, West Virginia 25301

WALTER F. GREELEY
EDWIN S. NAIL
Cabot Corporation
125 High Street
Boston, Massachusetts 02110

Attorneys for Appellant

Of Counsel:

WILLIAM G. CHARLTON
Cabot Corporation
Charleston National Plaza
Charleston, West Virginia 25302

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I. INTRODUCTION

Appellant, Cabot Corporation, appeals from the decision of the West Virginia Supreme Court of Appeals entered by an order of an evenly divided court, dated July 23, 1975, denying a petition for suspension and reversal of, and in effect affirming on the merits, the final order of the Public Service Commission of West Virginia in PSC Case No. 7612 dated June 13, 1975, fixing rates and charges for appellant's intrastate

gas utility operation in West Virginia. Appellant submits this Statement to show that the Supreme Court of the United States has jurisdiction of the appeal and that a substantial federal question is presented.[1]

2. OPINIONS BELOW

The final order of the West Virginia Supreme Court of Appeals filed July 23, 1975, is attached hereto as Appendix A. The final order of the Public Service Commission of West Virginia in PSC Case No. 7612 dated June 13, 1975, not yet reported, is attached hereto as Appendix B.

3. JURISDICTION

(a) The jurisdiction of this Court to review the decision of the West Virginia Supreme Court of Appeals is conferred by Title 28, United States Code, Section 1257(2). The final order of the Public Service Commission dated June 13, 1975, being legislative in nature and made by an instrumentality of the state, is a state law. As such, the order of the West Virginia Supreme Court of Appeals denying the petition for suspension and reversal of the Commission order constituted a judgment on the merits upholding the Commission's order (statute) against the appellant's claim of invalidity under the 14th Amendment to the United States Constitution. The Supreme Court's jurisdiction of this case by appeal is well established. *Atchison, Topeka & Santa Fe Railway Co.* v. *Public Utilities*

[1] True Temper Corporation was an Intervenor in the Public Service Commission proceeding. Park Corporation also intervened but withdrew as an Intervenor at the hearing held January 24, 1975.

Commission of the State of California, 346 U.S. 346 (1953); *Live Oak Water Users' Assoc.* v. *Railroad Comm'n,* 269 U.S. 354 (1926); *Napa Valley Elec. Co.* v. Railroad Comm'n, 251 U.S. 366 (1920); *Lake Erie & W.R. Co.* v. *Public Utilities Comm'n,* 249 U.S. 422 (1919).

(b) The judgment of the Supreme Court of Appeals of West Virginia sought to be reviewed was made and entered on July 23, 1975. Appellant's Notice of Appeal, attached hereto as Appendix C, was filed in the office of the Clerk of the Supreme Court of Appeals of West Virginia on August 18, 1975 (that court then having custody of the record), and copies were served on the same day on the appellees herein and Park Corporation.

4. THE INVALID STATUTE AND THE RELEVANT CONSTITUTIONAL PROVISIONS AND OTHER STATUTES

The statute asserted to be invalid is the final order of the Public Service Commission of West Virginia (hereinafter the "Commission") dated and entered on June 13, 1975, attached hereto as Appendix B, fixing the maximum rates and charges appellant's intrastate gas utility operation may charge its customers served under general tariffs. This statute is violative of the prohibition of the Fourteenth Amendment that:

> "[N]or shall any state deprive any person of life, liberty or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the law."

Although not asserted to be invalid, other relevant state and federal statutes include:

(a) Provisions of the West Virginia Code of 1931, as amended, attached hereto as Appendix D:

(i) Chapter 24, Article 2, Section's 2, 3 and 4, delegating to the Commission the power to fix utility rates;

(ii) Chapter 24, Article 5, Section 1, providing the sole and exclusive procedure for judicial review of a Commisson order;

(b) Provisions of the Internal Revenue Code (Title 26 of the U.S. Code) relating to foreign tax credits, attached hereto as Appendix E:

(i) 26 U.S.C. Sec. 901, which contains the basic provision permitting qualified persons an election to take a credit for qualified foreign taxes. This section also contains the provision for allowance of credit for foreign taxes deemed to have been paid under Section 902;

(ii) 26 U.S.C. Sec. 902, which contains the basic provision applicable to foreign taxes deemed paid in connection with the earnings of a foreign subsidiary or affiliate from which dividends received are required to be "grossed up" to the pre-tax amount of foreign profits distributed;

(iii) 26 U.S.C. Sec. 903, which provides that taxes imposed by a foreign country in lieu of income, profits or excess profit taxes shall also qualify for use as credits;

(iv) 26 U.S.C. Sec. 904, which provides various limitations on the amount of foreign taxes which can be credited against the U.S. tax. This section limits the foreign tax credit to the amount of U.S. taxes attributable to the taxpayer's foreign source income. Bittker & Eustice, *Federal Income Taxation of Corporations and Shareholders,* 17-31, 32 (3d ed., Warren, Gorham & Lamont, Inc., 1971);

(v) 26 U.S.C. Sec. 78, which requires the taxpayer to include in foreign source taxable income the foreign taxes allowable as a credit with respect to dividends received.

5. QUESTION PRESENTED

Whether, in fixing rates and charges for an intrastate gas producing and distributing public utility operation of a United States corporation which, alone and through subsidiaries, also does business in foreign countries, a state regulatory commission may use "foreign tax credits" to reduce the allowance for federal income taxes in determining the utility's cost of service from the statutory rate of 48 percent to 12.125 percent on the taxable income of the domestic intrastate utility operation without taking appellant's property for public use without just compensation in violation of the Fourteenth Amendment, when (a) the Internal Revenue Code does not permit the use of "foreign tax credits" to discharge or reduce federal income tax liability arising from domestic source taxable income; and (b) the rate of return found by the Commission to be fair (i.e., 8.75 percent on a depreciated original cost rate base) was not only lower than any fair return supported by the evidence, but cannot be earned because of the Commission's approach to pro forma federal income taxes.

6. STATEMENT OF THE CASE

(a) As a part of one of its divisions, appellant owns and operates in West Virginia an intrastate natural gas utility, which produces, purchases, and distributes natural gas to some 22,000 customers in nine West Virginia counties (hereinafter "Cabot utility") under regulation by the Commission. Alone among major

gas distributors in West Virginia, Cabot utility has not, as yet, been required to curtail service.

On February 1, 1973, Cabot utility filed with the Commission tariff amendments increasing rates charged customers served under its tariffs an average of 19 percent, effective March 19, 1973. The Commission suspended the use of the increased rates until July 6, 1973, pending Commission investigation and public hearing. Pursuant to state law, Cabot utility was permitted to place the increased rates into effect July 6, 1973, under bond in the principal sum of $530,000, conditioned to require refund, with interest, of any of the increased charges not ultimately allowed. After audit and investigation by Commission staff, the case was set for public hearing. Hearings were held on December 11, 1974, and January 24, 1975. There were initially two intervenors, True Temper Corporation and Park Corporation. Park Corporation withdrew as an intervenor at the January, 1975, hearing.

There were no material issues developed by the evidence except (1) Cabot utility's proposed design of rate blockings, which was opposed by the intervenor, True Temper Corporation, supported by the Commission staff, and approved by the Commission's Order; (2) the rate of return on depreciated original cost rate base required to attract utility capital, service the utility's allocable portion of appellant's debt and provide a reasonable return to the equity owners—the expert witness sponsored by Cabot utility being of opinion that an overall return of 9.75 percent to 10 percent was required to provide a fair and reasonable return and the expert witness sponsored by the Commission staff being of opinion that a 9.05 percent to 10 percent overall return would constitute a fair return; (3) in

calculating the cost of service element represented by pro forma federal income taxes which would be incurred on the taxable income of the Cabot utility, appellant's evidence was that the 48 percent statutory rate was the proper measure of Cabot utility's pro forma federal income tax liability, while the Commission staff, although accepting as correct appellant's 1972 consolidated tax return and its calculation of a federal income tax liability of $6,157,652, representing a 48 percent effective rate, for rate making purposes reduced the effective rate to 12.13536 percent in the following manner (Matthews—Cabot Request Exhibit No. 2, Sheet 2):

1. Federal Income Tax Liability	$6,157,652
2. Foreign Tax Credit	4,600,902
3. Tax Savings Item 2 ÷ Item 1 =	74.718%
4. Current Tax Rate	48.00000%
5. Tax Savings at (48% x 74.718%)	35.86464%
Net Current Tax Rate (48%-35.86464%)	12.13536%

The Commission staff accounting witness and the Commission ignored, as irrelevant, the fact that, of appellant's 1972 taxable income of $12,835,219, domestic sources contributed $1,185,599 and foreign sources contributed $11,649,620 (grossed up to include $4,600,-902 in foreign taxes claimed as a credit). Neither the Commission nor its accounting staff considered relevant the Internal Revenue Code provisions limiting the use of foreign tax credits to that portion of the U.S. income tax liability which resulted from foreign source taxable income.

(b) The Commission's Order (statute) of June 13, 1975, stating the tax issue to be "the proper handling

of Federal Income Tax and its application to foreign tax credits," held:

> "This Commission has a long standing policy of not allowing as an expense item taxes other than those actually paid to the Federal Government . . . . The Commission's basic philosophy is that the company can't pass on to the rate payers the obligation of taxes that haven't actually been paid to the [Federal] Government."

The Commission thus accepted the staff position that Cabot utility had an effective federal income tax rate of 12.13536 percent.

The Commission's Order, while acknowledging that appellant's evidence was that a fair rate of return was in the range of 9.75 percent to 10 percent and that "the staff recommended a return of 9.05 percent to 10 percent," nevertheless held that an 8.75 percent return on Cabot utility's depreciated original cost rate base will permit the Cabot utility "to render reliable service to its customers at just and reasonable rates and should be adequate to allow the company to maintain its credit standing and to attract necessary capital for said purpose."

(c) *The impact of the Commission's Order.* The Commission accepted the cost of service data of its accounting staff, subject to the adjustments set forth in the Order. The staff accounting exhibits assumed, for illustrative purposes only, a rate of return of 8.5 percent. If line 15, column 2 ("balance of return after tax") of Staff Exhibit No. 1, Statement D, attached hereto as Appendix F, is adjusted by increasing the $353,814 to $367,003 to reflect the increase of the rate of return to 8.75 percent from the 8.5 percent assumed

return in accordance with the Commission's Order and if related adjustments are made, the mathematical calculation of the impact of a federal income tax rate of 12.13536 percent as opposed to a 48 percent rate may be easily demonstrated:

1. Taxable income (Source: Line 16, Col. 2, St. D, Staff Ex. 1, adjusted per Order by adding $13,189 additional return and $1,820 additional income tax)	$417,690
2. Federal income tax at statutory corporate rate ($417,690 x 48%)	200,491
3. Federal income tax per staff computation (Source: Line 18, Col. 2, St. D, Staff Ex. 1, adjusted to reflect taxable income of $417,690 x .1213536 = $50,688	50,688
4. Difference between federal income tax at the statutory rate of 48% and at the rate of 12.13536% computed per staff approach	149,803

From this computation it is obvious that the rates approved by the Commission to yield the after tax balance for return of $367,003 will actually produce only $217,200 as an after tax balance for return if the statutory rate of 48 percent is applied to determine the amount of federal income tax. This reduces the rate of return to 7.4 percent.

(d) *The Federal Question and How Raised.* In appellant's petition to the Supreme Court of Appeals of West Virginia, dated and filed July 11, 1975, seeking judicial review of the Commission's order of June 13, 1975, appellant stated that the first question presented was whether or not the Commission's treatment of federal income tax expense "constitutes the taking of petitioner's property for public use without just com-

pensation in violation of the 14th Amendment to the United States Constitution. . .'' Review by the Supreme Court of Appeals is the exclusive judicial review provided by West Virginia law to those aggrieved by rate orders of the Commission. The West Virginia Supreme Court of Appeals, by an evenly divided court, denied appellant's petition, thus upholding the Commission's Order against appellant's claim of violation of the Fourteenth Amendment.

7. REASONS FOR PLENARY CONSIDERATION OF THE APPEAL.

A diligent search has failed to disclose any reported case in which a federal or state regulatory commission or court (except in West Virginia) has ever considered whether foreign tax credits can be used to reduce the allowance for federal income taxes on U.S. domestic source income in a utility rate proceeding.

This country's privately owned public utility industry is in serious trouble, primarily because the traditional use of a historic test year to determine utility cost of service, while suitable in a stable, non-inflationary economy, produces rates inadequate to cover the rapidly increasing costs experienced in the 1970's. In the natural gas industry, the problem is made more serious by a shortage of natural gas—a problem which appellant, alone among West Virginia's major gas distributing utilities, has thus far managed to solve without curtailing service to its customers.

The importance of this case is not only that the West Virginia Commission fixed rates insufficient to provide Cabot utility a reasonable return, but also that the Commission has established a precedent which makes it impossible in this case and in future cases, absent

reversal by this Court, to obtain recognition of that portion of appellant's actual cost of service represented by federal income taxes.

By reducing Cabot utility's effective federal income tax rate from the statutory rate of 48 percent to 12.135 percent solely by holding that foreign taxes paid by appellant will not be recognized as a cost, but that the resulting foreign tax credits for taxes actually paid effect a 74.718 percent ''tax savings'' in taxes actually paid to the United States Government (which are the only taxes which will be recognized as a cost of service), the Commission acted arbitrarily and capriciously and without any basis in law or reason. The end result of the Commission's Order is to reduce Cabot utility's return from the 8.75 percent the Commission found fair and reasonable (which was less than the minimum of 9.05 percent supported by the expert witness sponsored by the Commission staff) to 7.4 percent. Since appellant's embedded cost of long term debt was 9.30 percent in fiscal year 1973 an overall return of 7.4 percent will produce an even lower return on appellant's equity investment. Such end result is confiscatory, unjust and unreasonable and is not in accord with the decision of this Court in *F.P.C.* v. *Hope Natural Gas Co.,* 320 U.S. 591 (1944), and other applicable cases.

The requirement that all ''taxes'' be included in utility operating expenses and deducted from utility revenues to calculate the actual return on utility property was established in an opinion by Justice Brandeis speaking for a unanimous court in *Galveston Elec. Co.* v. *City of Galveston,* 258 U.S. 388, 399 (1922), and followed in *Georgia Ry. & Power Co.* v. *Railroad Comm'n,* 262 U.S. 625, 633 (1923), and is now uni-

versally accepted. 1 Priest, *Principles of Utility Regulation* 51, 52 (Michie 1969). The Supreme Court of Kansas articulated the importance of the rule in *Southwestern Bell Tel. Co.* v. *Kansas State Corp. Comm'n,* 192 Kan. 39, 386 P.2d 515, 543 (1963), in these words:

> "State and federal income tax is the most important item of expense to be considered in the determination of a fair return. This exceeds all classified expenses other than maintenance. Income tax expense amounts to approximately 52 per cent [now 48%] of the company's net income. For every $1,000,000 the company is allowed to earn as a fair return, an additional $1,150,000 [now $923,077] must be allowed for income tax expense. Income tax is charged as an expense in calculating the rate to the subscribers, and is not considered as equity capital or stockholders' expense for the purpose of public utility regulation."

The foreign tax credit has been part of the United States tax law since the Revenue Act of 1918. 40 Stat. 1057-1152. Under the tax laws of the United States, domestic corporations are subject to tax on their world wide income, irrespective of its geographic source.

> "The purpose of the foreign tax credit is to eliminate double taxation of foreign source income. In effect, the foreign tax is treated as a down payment on the domestic tax payer's United States tax liability with respect to that income." Bittker and Eustice, *Federal Income Taxation of Corporations and Shareholders* 17-26 (3d ed., Warren, Gorham & Lamont, 1971).

The evidence in this case discloses that Cabot utility requires substantial additional capital investment if

it is to continue to provide its customers with adequate service. This utility cannot attract capital and provide reasonable earnings for its equity investors if it is limited to rates which would produce only a 7.4 percent rate of return on the depreciated original cost of its utility investment. The Commission itself has determined that a fair rate of return is 8.75 percent, but by its arbitrary and capricious determination that federal income tax expense is only 12.135 percent of taxable income has taken appellant's property for public use without just compensation in violation of the 14th Amendment to the Constitution of the United States, and contrary to applicable decisions of this Court.

CONCLUSION

It is submitted that the question presented by this appeal is substantial and of public importance.

Respectfully submitted,

F. PAUL CHAMBERS
MICHAEL A. ALBERT
1601 Kanawha Valley Building
Charleston, West Virginia 25301

WALTER F. GREELEY
EDWIN S. NAIL
Cabot Corporation
125 High Street
Boston, Massachusetts 02110

Attorneys for Appellant

Of Counsel:

WILLIAM G. CHARLTON
Cabot Corporation
Charleston National Plaza
Charleston, West Virginia 25302

October 21, 1975

APPENDIX

APPENDIX A

Final Order of West Virginia Supreme Court of Appeals of July 23, 1975

STATE OF WEST VIRGINIA

At a Regular Term of the Supreme Court of Appeals continued and held at Charleston, Kanawha County, on the 23rd day of July, 1975, the following order was made and entered, to-wit:

CABOT CORPORATION

v.

PUBLIC SERVICE COMMISSION OF WEST VIRGINIA

Upon an appeal from, suspension and review of the final order of the Public Service Commission of West Virginia made an entered on June 13, 1975.

The Court, having maturely considered the petition and exhibit, note of argument in support thereof; the record consisting of all papers, documents and evidence which were before the Public Service Commission at the hearing which resulted in the entry of the final order complained of; the Statement of reasons for the entry of its order of the 13th day of June, 1975, filed herein by the respondent, Public Service Commission of West Virginia, on July 21, 1975; and the oral argument of counsel on the 22d day of July, 1975, the date fixed by the Court for hearing upon the aforesaid petition; is of opinion that the petitioner has not shown itself entitled to the relief prayed for in its said petition. It is therefore considered and ordered that the prayer of the petition for an appeal from, suspension and review, in this proceeding, be, and the same is hereby, denied by an equally divided Court. Justices Sprouse and Neely would grant. Justice Caplan absent.

It is further ordered that leave be, and the same is hereby granted to the Public Service Commission of West Virginia to withdraw from the office of the Clerk of this Court, the record consisting of all papers, documents and evidence originally filed with the Public Service Commission of West Virginia.

A True Copy

Attest: GEORGE W. SINGLETON

Clerk Supreme Court of Appeals

APPENDIX B

Final Order of Public Service Commission of West Virginia of June 13, 1975

PUBLIC SERVICE COMMISSION
OF WEST VIRGINIA
CHARLESTON

At a session of the PUBLIC SERVICE COMMISSION OF WEST VIRGINIA at the Capitol in the City of Charleston on the 13th day of June, 1975.

CASE No. 7612

CABOT CORPORATION, a corporation.

In the matter of increased rates and charges

PROCEDURE

On the 1st day of February, 1973, Cabot Corporation, a corporation, filed its tariff designated 6th Revision of Original Sheet No. 6, canceling 5th Revision of Original Sheets No. 6, and 3rd Revision of Original Sheet No. 8, canceling 2nd Revision of Original Sheet No. 8, to its Tariff P.S.C. W.Va. No. 1, stating an increase of approximately nineteen per cent (19%) in rates and charges for furnishing gas service to its customers in the entire territory served by it in the State of West Virginia, to become effective March 19, 1973.

By order entered herein on March 2, 1973, Cabot Corporation, a corporation, was made respondent to this proceeding and pending investigation, hearing and decision, the aforesaid revised tariff was suspended and the use of the rates and charges stated therein deferred until the 6th day of July, 1973, unless otherwise ordered by the Commission.

By order entered herein on June 5, 1973, Cabot Corporation, a corporation, was authorized to place into effect the increased rates contained in the aforesaid revised tariff after filing a bond in the amount of Five Hundred Thirty Thousand Dollars ($530,000), pursuant to Chapter 24, Article 2, Section 4, of the Code of West Virginia.

By order entered herein on October 9, 1974, this matter was set for hearing to be held in the Commission's Hearing Room at the Capitol in the City of Charleston on the 11th day of December, 1974, at 10:00 A.M., EST, at which time and place the respondent was directed to appear and offer evidence in support of its aforesaid increased rates and charges and anyone might appear and make such objection thereto as may be deemed proper.

The order further provided that the respondent give notice of the filing of the aforesaid revised tariff and of the time and place of hearing thereon by posting a copy of said order at each of its offices where bills for gas service are paid for a period of at least twenty (20) days prior to the 11th day of December, 1974, for public inspection; and by publishing a copy of the order once a week for two (2) successive weeks, the first publication to be made not more than thirty (30) days nor less than fifteen (15) days prior to the 11th day of December, 1974, in newspapers published and of general circulation in the Counties of Kanawha, Wirt, Wyoming, Calhoun, Raleigh, Summers, Fayette, Wood and McDowell, making due return thereof to the Commission on or before the day of hearing.

Hearing was held on December 11, 1974, at which F. Paul Chambers, Charles Q. Gage, and William W. Hensley appeared as counsel for the respondent; Howard R. Klostermeyer, John H. Tinney, and Jack E. Shelley appeared as counsel for True Temper Corporation, an intervenor; and H. Thomas Vanderford appeared as counsel for Park Corporation, an intervenor. The staff of the Commission

was represented by Marian W. Louis, Legal Division; Jack Vickers, Division of Engineering; and James C. Matthews and Laxmi N. Mehra, Division of Accounts, Finance and Rates. There were numerous letters of protest, as well as a petition, lodged in the file; however, none of the parties appeared in person at the hearing. It appearing that the posting and publication requirements were made in accordance with the Commission's order, evidence was presented and the case was continued to the 24th day of January, 1975, at 10:00 A.M.

The hearing was resumed on January 24, 1975, at which F. Paul Chambers and Michael A. Albert appeared as counsel for the respondent; Howard R. Klostermeyer, John H. Tinney, and Jack E. Shelley appeared as counsel for True Temper Corporation, an intervenor; and H. Thomas Vanderford appeared as counsel for Park Corporation, an intervenor. The staff of the Commission was represented by Thomas N. Hanna, Legal Division; Jack Vickers, Division of Engineering; and James C. Matthews and Laxmi N. Mehra, Division of Accounts, Finance and Rates. At this hearing Charleston Ordnance Center, by its counsel, moved to withdraw and to be relieved from further participation in this action as an intervenor. This motion was granted and further evidence was presented, at the conclusion of which the case was submitted for decision, subject to the filing of briefs.

Evidence

Cabot Corporation sells gas at retail to customers in Kanawha, Wirt, Wyoming, Calhoun, Raleigh, Summers, Fayette, Wood, and McDowell Counties, in West Virginia, to residential, commercial, and small industrial customers aggregating approximately 22,000 users. For many years the principal business of the respondent was the manufacture of carbon black and the production of petroleum and natural gas which was primarily used as a feed stock

in its manufacture of carbon black. When it started selling gas to retail customers in West Virginia it did not organize a subsidiary corporation for that purpose but has since established a gas marketing division which includes the West Virginia utility operation plus two corporate subsidiaries, Industrial Gas Corporation and Mountain Gas Company, both of which are interstate gas pipelines. The Cabot Corporation is a multinational corporation which alone, or through its subsidiaries, has plants and operations in more than ten foreign countries. The sales of Cabot and its subsidiaries in the fiscal year 1974 totaled slightly over $400,000,000. West Virginia is the only State in which Cabot operates a gas distribution utility, it being the third largest gas distribution utility in the State. The gas utility has an integrated pipeline system with a large number of wells in the numerous areas of gas supply connected to general service customers in the vicinity of Elizabeth, Grantsville, Sissonsville, Charleston, Glasgow, Montgomery, Gauley Bridge, Fayetteville, Oak Hill, Mount Hope, and Hinton, and though other gas companies in West Virginia are presently suffering from a shortage of supply, this company has not required curtailment of any of its residential, commercial, or industrial users prior to its filing in this case. The respondent's tariff contained six rate blocks and gave to the larger consumer of natural gas a substantial reduction in cost per Mcf. The new tariff that was filed in this case contains three rate blocks that increase residential rates 15.37%, commercial rates 22.25%, and industrial rates by 43.93%, respondent thereby taking the position that the old rate blocking which was designed to encourage use of large quantities of gas is no longer appropriate and that the new rate structure should encourage conservation of the gas supply. Cabot's gas utility customers are of two classes, the first being tariff customers or general service customers consisting of residential, commercial, and small industrial users, and the second being the large industrials and sales for resale

customers who obtain gas from the respondent under special contracts.

True Temper Corporation, a subsidiary of Allegheny Ludlum Corporation, an intervenor in this proceeding, objected to the percentage increase of 54.89% that the proposed rates would inflict upon it and contended that the requested three-block rate design is not cost related and does not equitably distribute respondent's cost of service among all of its customers. This intervenor also questioned the propriety of the use of a rate design based upon conserving natural gas when the respondent was not in a position where it had been required to curtail its gas deliveries.

A comparison of respondent's Exhibit No. 3 and staff Exhibit No. 1 reflects a number of minor differences in operation and maintenance expenses, depreciation expenses and taxes; due to the staff's elimination of certain claimed expenses and a difference in approach in the method of allocation of these expenses among customers. This portion of the cost of service as computed and allocated by staff was accepted by the respondent, leaving little difference in accounting results except where it related to respondent's Federal Income Tax Liability and the proper treatment of consolidated tax savings and its application of foreign tax credits.

Comments and Findings

This case presents three issues of substance for the Commission to decide, they being: (1) the proper handling of Federal Income Tax and its application of foreign tax credits, (2) determining a fair rate of return on respondent's utility investment, and (3) cost assignment among classes of customers.

(1) In the matter of computation of Federal Income Tax, the respondent contends that the gross income tax liability, before any tax savings due to filing a consolidated

return and/or foreign tax credits which are treated as a direct reduction of Federal Income Tax liability, should be applied to its West Virginia utility operations. The staff on the other hand in its computation has used only the actual tax paid to the United States Government in its cost of service. This Commission has a long-standing policy of not allowing as an expense item taxes other than those actually paid to the Federal Government. It has never allowed income tax recovery to be more or less than the tax paid and in Case No. 6609 (1970) ARPSCWV, Page 128, being a proceeding involving the Cabot Corporation, the Commission held that expense credit for Federal Income Tax should be disallowed where the utility paid no taxes due to foreign tax credits. We have before us no evidence which will persuade the Commission to depart from its former position in this matter; therefore, in this instance we will allow in staff's computation of "cost of service" the actual income taxes paid by the company in keeping with our previous treatment of income tax as an item of expense. The Commission's basic philosophy is that the company can't pass on to the rate payers the obligation of taxes that haven't actually been paid to the Government.

(2) Regarding the determination of a fair rate of return on respondent's utility investment the respondent contends that a fair rate of return should be in the range of 9.75% to 10% and the staff recommended a return of 9.05% to 10%. Cabot's rate of return witness stated that since the corporation does not borrow funds on an independent basis, it was difficult to construct historical coverage of interest charges for the gas utility operation in view of the fact that division also did not have a separate earned surplus account or a capital stock account. He further stated that an attempt to assemble separate figures for the gas utility business would require considerable judgment on allocation of the Cabot Corporation accounts and would not result in a typical gas utility capitalization. Faced with this situation an accurate debt ratio cannot be determined for the gas utility portion of Cabot Corporation and a debt ratio of 24%, being the ratio for the parent company, would have to be used, this ratio being considerably below the 54% average debt ratio of the 22 utility companies included in Mr. Leness' study. In determining the average cost of long-term debt that would also have to be based on the cost of debt to the Cabot Corporation and would not be specific or accurate as to the gas utility division.

In arriving at a fair rate of return the Commission is being required to make a judgment based upon the foregoing items plus the business risks of the current inflationary period, current trends in the money market and the historical factors, none of which items can be accurately determined insofar as the respondent is concerned. A just and reasonable rate of return can only be determined in light of all of these factors and the evidence and cannot be computed to a precise mathematical formula. After considering the cost of capital and all other factors and applying it to the test period herein we find that the respondent should be given the opportunity to earn an 8.75% return upon staff's adjusted rate base of $11,262,393, and that such a rate of return will permit the company to render reliable service to its customers at just and reasonable rates and should be adequate to allow the company to maintain its credit standing and to attract necessary capital for said purposes.

(3) Based on the theory that each class of customer should pay the total cost of service allocated to it by acceptable methods the staff, assuming a rate of return of 8.50% as approved by the Commission in the last rate case involving the respondent, arrived at a total cost of serving its residential, commercial, and small (Class I) industrial customers of $3,622,271 compared to revenues from these customers of $3,221,936, or a deficiency of $400,335.

The Commission accepts the staff allocation of cost of service with the exception that the rate of return should be 8.75% rather than 8.50% on a net original cost rate base. This change results in a cost of service to the above mentioned customers as follows:

Cost of service per staff at 8.50%	$3,622,271
Increase in rate of return from 8.50% to 8.75%	13,189
Increase in Federal Income Tax	1,820
Total cost of service per Commission decision	3,637,280
Less revenues at prior rates	3,221,936
Adjusted deficiency	415,344
Additional Business and Occupation Tax at 4.29%	18,617
Total gross deficiency	433,961

True Temper Corporation, a subsidiary of Allegheny Ludlum Corporation, an intervenor in this matter, objects to the percentage increase of 54.89% that it will have to pay under the requested rates and contends that the three-block rate design used by respondent is not cost related and doesn't reflect accurately a fair distribution of costs among all of the utility's customers. This intervenor also takes the position that the gas company should not be permitted to design rates that would encourage conservation until such time as the gas company is placed in a position of curtailment due to a lack of supply. A cost of service study made by staff accountant Matthews reflects that True Temper Corporation under present rates, as increased by 30-B proceedings, did not pay its cost of service by a deficiency of $58,000 during the test year; therefore, it does appear that to maintain their rates at the current level would necessitate subsidization of True Temper to a degree by the other customers of Cabot. To require a company to be in a curtailment posture as a prerequisite to its being allowed to design rates to encourage conservation in the face of the present nationwide gas shortage would be improper and inequitable. We find that True Temper's objection to the percentage rate increase imposed upon them by the proposed three-block rate design is not well founded, since the cost of service study discloses that the present rates charged True Temper did not cover the cost of serving it during the test year and that the proposed increase to this user does not cover this deficit.

Respondent's rates and charges last approved by the Commission are unjust and unreasonable in that they will not produce sufficient revenues to enable the respondent to pay its reasonable and necessary operating expenses and taxes, provide for depreciation, and earn a fair return on its property used and useful in its public service business.

The rates and charges that have been placed in effect under bond are likewise unjust and unreasonable in that they will produce more revenues than are needed for the aforesaid purposes.

Rates designed to produce the additional amount of the gross deficiency set forth herein of $433,961 should be approved and they should produce revenues sufficient, but not more than sufficient, for the aforesaid purposes.

The three-block rate design requested by respondent should be approved by the Commission.

ORDER

1. IT IS ORDERED that the rates and charges that respondent now has in effect under bond be, and they are hereby, canceled and stricken from the tariff files of the Commission.

2. IT IS FURTHER ORDERED that respondent design rates that will produce additional revenues of $433,961, this new tariff to be designed in accordance with the findings of this Commission and that this tariff shall be submitted to the Commission for its approval on or before August 1, 1975,

and if approved it shall be placed in effect as of July 6, 1973.

3. It Is Further Ordered that the respondent refund to the persons or parties entitled thereto within 120 days of the date of this order the difference between the amount collected under the rates placed in effect under bond and the amount which would have been collected under the rates that are herein approved, with interest thereon at the rate of six per cent (6%) per annum until paid, and shall report to the Commission the amount refunded, including interest, the manner of refunding, and the amount, if any, which it has been unable to refund.

4. It Is Further Ordered that the respondent file with the Commission tariff sheets stating the rates and charges herein approved.

A Copy.

Teste:

/s/ S. Grover Smith, Jr.
S. Grover Smith, Jr.
Secretary

APPENDIX C

Notice of Appeal

IN THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

Cabot Corporation, *Appellant,*

v.

Public Service Commission of West Virginia, *Appellee.*

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

Notice is hereby given that Cabot Corporation, the appellant above named, hereby appeals to the Supreme Court of the United States from the final judgment of the Supreme Court of Appeals of West Virginia, entered in this action on July 23, 1975, denying the petition of Cabot Corporation for an appeal from, suspension and reversal of, the final order dated June 13, 1975, of the Public Service Commission of West Virginia in PSC Case No. 7612 which denial by the Court constituted an affirmance of said order of the Public Service Commission.

This appeal is taken pursuant to 28 U.S.C. § 1257(2).

/s/ F. Paul Chambers
Counsel for Appellant,
Cabot Corporation.

[Certificate of Service Omitted]

APPENDIX D

West Virginia Code of 1931, as Amended, Chapter 24, Article 2, Sections 2, 3 and 4 and Chapter 24, Article 5, Section 1

§ 24-2-2. General power of commission to regulate public utilities.

The commission is hereby given power to investigate all rates, methods and practices of public utilities subject to the provisions of this chapter; to require them to conform to the laws of this State and to all rules, regulations and orders of the commission not contrary to law; and to require copies of all reports, rates, classifications, schedules and timetables in effect and used by such utility or other person, to be filed with the commission, and all other information desired by the commission relating to such investigation and requirements, including inventories of all property in such form and detail as the commission may prescribe. The commission may compel obedience to its lawful orders by mandamus or injunction or other proper proceedings in the name of the State in any circuit court having jurisdiction of the parties or of the subject matter, or the supreme court of appeals direct, and such proceedings shall have priority over all pending cases. The commission may change any intrastate rate, charge or toll which is unjust or unreasonable or any interstate charge with respect to matters of a purely local nature which have not been regulated by or pursuant to act of Congress and may prescribe such rate, charge or toll as would be just and reasonable, and change or prohibit any practice, device or method of service in order to prevent undue discrimination or favoritism between persons and between localities and between commodities for a like and contemporaneous service. But in no case shall the rate, toll or charge be more than the service is reasonably worth, considering the cost thereof. Every order entered by the commission shall continue in force until the expiration of the time, if any,

named by the commission in such order, or until revoked or modified by the commission, unless the same be suspended, modified or revoked by order or decree of a court of competent jurisdiction. (1913, c. 9, § 5; 1915, c. 8, § 5; Code 1923, c. 15-O, § 5; 1935, c. 115.)

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§ 24-2-3. General power of commission with respect to rates.

The commission shall have power to enforce, originate, establish, change and promulgate tariffs, rates, joint rates, tolls and schedules for all public utilities except carriers by vehicles over streets and roads, including municipalities supplying gas, electricity or water. And whenever the commission shall, after hearing, find any existing rates, tolls, tariffs, joint rates or schedules unjust, unreasonable, insufficient or unjustly discriminatory or otherwise in violation of any of the provisions of this chapter, the commission shall by an order fix reasonable rates, joint rates, tariffs, tolls or schedules to be followed in the future in lieu of those found to be unjust, unreasonable, insufficient or unjustly discriminatory or otherwise in violation of any provisions of law, and the said commission, in fixing the rate of any railroad company, may fix a fair, reasonable and just rate to be charged on any branch line thereof, independent of the rate charged on the main line of such railroad. (1915, c. 8, § 22; Code 1923, c. 15-O, § 22.)

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§ 24-2-4. Procedure for changing rates.

No public utility subject to this chapter shall change, suspend or annul any rate, joint rate, charge, rental or classification except after thirty days' notice to the commission and the public, which notice shall plainly state the changes proposed to be made in the schedule then in force and the time when the changed rates or charges shall go into effect. But the commission may enter an order suspending the

proposed rate as hereinafter provided. The proposed changes shall be shown by printing new schedules, or shall be plainly indicated upon the schedules in force at the time, and kept open to public inspection: Provided, however, that the commission may, in its discretion, and for good cause shown, allow changes upon less time than the notice herein specified, or may modify the requirements of this section in respect to publishing, posting and filing of tariffs, either by particular instructions or by general order.

Whenever there shall be filed with the commission any schedule stating a change in the rates or charges, or joint rates or charges, or stating a new individual or joint rate or charge or joint classification or any new individual or joint regulation or practice affecting any rate or charge, the commission shall have authority, either upon complaint or upon its own initiative without complaint, to enter upon a hearing concerning the propriety of such rate, charge, classification, regulation or practice; and, if the commission so orders, it may proceed without answer or other form of pleading by the interested parties, but upon reasonable notice, and, pending such hearing and the decision thereon, the commission, upon filing with such schedule and deliver ing to the public utility affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, regulation or practice, but not for a longer period than one hundred and twenty days beyond the time when such rate, charge, classification, regulation or practice would otherwise go into effect; and after full hearing, whether completed before or after the rate, charge, classification, regulation or practice goes into effect, the commission may make such order in reference to such rate, charge, classification, regulation or practice as would be proper in a proceeding initiated after the rate, charge, classification, regulation or practice had become effective: Provided, that if any such hearing and decision thereon

cannot be concluded within the period of suspension, as above stated, such rate, charge, classification, regulation or practice shall go into effect at the end of such period. In such case the commission may require such public utility to enter into a bond in an amount deemed by the commission to be reasonable and conditioned for the refund to the persons or parties entitled thereto of the amount of the excess, plus interest at the rate of six percent per annum, if such rates so put into effect are subsequently determined to be higher than those finally fixed for such utility. No such accrued interest paid shall be deemed part of the cost of doing business in a subsequent application for changing rates or any decision thereon. At any hearing involving a rate sought to be increased or involving the change of any fare, charge, classification, regulation or practice, the burden of proof to show that the increased rate or proposed increased rate, or the proposed change of fare, charge, classification, regulation or practice is just and reasonable shall be upon the public utility making application for such change. When in any case pending before the commission all evidence shall have been taken, and the hearing completed, the commission shall, within three months, render a decision in such case.

Where more than twenty members of the public are affected by a proposed change in rates, it shall be a sufficient notice to the public within the meaning of this section if such notice is published as a Class II legal advertisement in compliance with the provisions of article three [§ 59-3-1 et seq.], chapter fifty-nine of this Code, and the publication area for such publication shall be the community where the majority of the resident members of the public affected by such change reside or, in case of non-residents, have their principal place of business within this State. (1913, c. 9, § 9; 1915, c. 8; § 9; 1921, c. 150, § 9; Code 1923, c. 15-O, § 9; 1953, c. 152; 1967, c. 105.)

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§ 24-5-1. Review of final orders of commission.

Any party feeling aggrieved by the entry of a final order by the commission, affecting him or it, may present a petition in writing to the supreme court of appeals, or to a judge thereof in vacation, within thirty days after the entry of such order, praying for the suspension of such final order. The applicant shall deliver a copy of such petition to the secretary of the commission before presenting the same to the court or the judge. The court or judge shall fix a time for the hearing on the application, but such hearing, unless by agreement of the parties, shall not be held sooner than five days after its presentation; and notice of the time and place of such hearing shall be forthwith delivered to the secretary of the commission, so that the commission may be represented at such hearing by one or more of its members or by counsel. If the court or the judge after such hearing be of the opinion that a suspending order should issue, the court or the judge may require bond, upon such conditions and in such penalty, and impose such terms and conditions upon the petitioner, as are just and reasonable. For such hearing the commission shall file with the clerk of said court all papers, documents, evidence and records or certified copies thereof as were before the commission at the hearing or investigation resulting in the entry of the order from which the petitioner appeals. The commission shall file with the court before the day fixed for the final hearing a written statement of its reasons for the entry of such order, and after arguments by counsel the court shall decide the matter in controversy as may seem to be just and right. (1913, c. 9, § 16; Code 1923, c. 15-O, § 16.)

APPENDIX E

Title 26 U.S. Code, Sections 78, 901-905, as Amended

§ 78. Dividends received from certain foreign corporations by domestic corporations choosing foreign tax credit

If a domestic corporation chooses to have the benefits of subpart A of part III of subchapter N (relating to foreign tax credit) for any taxable year, an amount equal to the taxes deemed to be paid by such corporation under section 902(a) (1) (relating to credit for corporate stockholder in foreign corporation) or under section 960(a)(1)(C) (relating to taxes paid by foreign corporation) for such taxable year shall be treated for purposes of this title (other than section 245) as a dividend received by such domestic corporation from the foreign corporation.

Added Pub. L. 87-834, § 9(b), Oct. 16, 1962, 76 Stat. 1001.

§ 901. Taxes of foreign countries and of possessions of United States

(a) Allowance of credit.—If the taxpayer chooses to have the benefits of this subpart, the tax imposed by this chapter shall, subject to the applicable limitation of section 904, be credited with the amounts provided in the applicable paragraph of subsection (b) plus, in the case of a corporation, the taxes deemed to have been paid under sections 902 and 960. Such choice for any taxable year may be made or changed at any time before the expiration of the period prescribed for making a claim for credit or refund of the tax imposed by this chapter for such taxable year. The credit shall not be allowed against the tax imposed by section 56 (relating to minimum tax for tax preferences), against the tax imposed for the taxable year under section 72(m)(5)(B) (relating to 10 percent tax on premature distributions to owner-employees), against the tax imposed by section 402(e) (relating to tax on lump sum distributions), against the tax imposed for the taxable

year by section 408(f) (relating to additional tax on income from certain retirement accounts), against the tax imposed by section 531 (relating to the tax on accumulated earnings), against the additional tax imposed for the taxable year under section 1333 (relating to war loss recoveries) or under section 1351 (relating to recoveries of foreign expropriation losses), or against the personal holding company tax imposed by section 541.

(b) Amount allowed.—Subject to the applicable limitation of section 904, the following amounts shall be allowed as the credit under subsection (a):

(1) Citizens and domestic corporations.—In the case of a citizen of the United States and of a domestic corporation, the amount of any income, war profits, and excess profits taxes paid or accrued during the taxable year to any foreign country or to any possession of the United States; and

(2) Resident of the United States or Puerto Rico.—In the case of a resident of the United States and in the case of an individual who is a bona fide resident of Puerto Rico during the entire taxable year, the amount of any such taxes paid or accrued during the taxable year to any possession of the United States; and

(3) Alien resident of the United States or Puerto Rico.—In the case of an alien resident of the United States and in the case of an alien individual who is a bona fide resident of Puerto Rico during the entire taxable year, the amount of any such taxes paid or accrued during the taxable year to any foreign country; and

(4) Nonresident alien individuals and foreign corporations.—In the case of any nonresident alien individual not described in section 876 and in the case of

any foreign corporation, the amount determined pursuant to section 906; and

(5) Partnerships and estates.—In the case of any individual described in paragraph (1), (2), (3), or (4), who is a member of a partnership or a beneficiary of an estate or trust, the amount of his proportionate share of the taxes (described in such paragraph) of the partnership or the estate or trust paid or accrued during the taxable year to a foreign country or to any possession of the United States, as the case may be.

(c) Similar credit required for certain alien residents.—Whenever the President finds that—

(1) a foreign country, in imposing income, war profits, and excess profits taxes, does not allow to citizens of the United States residing in such foreign country a credit for any such taxes paid or accrued to the United States or any foreign country, as the case may be, similar to the credit allowed under subsection (b) (3),

(2) such foreign country, when requested by the United States to do so, has not acted to provide such a similar credit to citizens of the United States residing in such foreign country, and

(3) it is in the public interest to allow the credit under subsection (b) (3) to citizens or subjects of such foreign country only if it allows such a similar credit to citizens of the United States residing in such foreign country,

the President shall proclaim that, for taxable years beginning while the proclamation remains in effect, the credit under subsection (b) (3) shall be allowed to citizens or subjects of such foreign country only if such foreign country, in imposing income, war profits, and excess profits taxes, allows to citizens of the United States residing in such foreign country such a similar credit.

(d) Corporations treated as foreign.—For purposes of this subpart, the following corporations shall be treated as foreign corporations:

(1) a corporation entitled to the benefits of section 931, by reason of receiving a large percentage of its gross income from sources within a possession of the United States; and

(2) a corporation organized under the China Trade Act, 1922 (15 U.S.C., chapter 4), and entitled to the deduction provided in section 941.

For purposes of this subpart, dividends from a DISC or former DISC (as defined in section 992(a)) shall be treated as dividends from a foreign corporation to the extent such dividends are treated under part I as income from sources without the United States.

(e) Foreign taxes on mineral income.—

(1) Reduction in amount allowed.—Notwithstanding subsection (b), the amount of any income, war profits, and excess profits taxes paid or accrued during the taxable year to any foreign country or possession of the United States with respect to foreign mineral income from sources within such country or possession which would (but for this paragraph) be allowed under such subsection shall be reduced by the amount (if any) by which—

(A) the amount of such taxes (or, if smaller, the amount of the tax which would be computed under this chapter with respect to such income determined without the deduction allowed under section 613), exceeds

(B) the amount of the tax computed under this chapter with respect to such income.

(2) Foreign mineral income defined.—For purposes of paragraph (1), the term "foreign mineral income"

means income derived from the extraction of minerals from mines, wells, or other natural deposits, the processing of such minerals into their primary products, and the transportation, distribution, or sale of such minerals or primary products. Such term includes, but is not limited to—

(A) dividends received from a foreign corporation in respect of which taxes are deemed paid by the taxpayer under section 902, to the extent such dividends are attributable to foreign mineral income, and

(B) that portion of the taxpayer's distributive share of the income of partnerships attributable to foreign mineral income.

(f) Cross reference.—

(1) For deductions of income, war profits, and excess profits taxes paid to a foreign country or a possession of the United States, see sections 164 and 275.

(2) For right of each partner to make election under this section, see section 703(b).

(3) For right of estate or trust to the credit for taxes imposed by foreign countries and possessions of the United States under this section, see section 642(a) (2).

(4) For reduction of credit for failure of a United States person to furnish certain information with respect to a foreign corporation controlled by him, see section 6038.

Aug. 16, 1954, c. 736, 68A Stat. 285; Sept. 14, 1960, Pub.L. 86-780, § 3(a), (b), 74 Stat. 1013; Oct. 16, 1962, Pub.L. 87-834, §§ 9(d)(3), 12(b)(1), 76 Stat. 1001, 1031; Feb. 26, 1964, Pub.L. 88-272, Title II, § 207(b)(7), 78 Stat. 42; Apr. 8, 1966, Pub.L. 89-384, § 1(c)(2), 80 Stat. 102; Nov. 13, 1966,

Pub.L. 89-809, Title I, § 106(a)(4), (5), (b)(1), (2), 80 Stat. 1569; Dec. 30, 1969, Pub.L. 91-172, Title III, § 301(b)(9), Title V, § 506(a), 83 Stat. 585, 634; Dec. 10, 1971, Pub.L. 92-178, Title V, § 502(b)(1), 85 Stat. 549; Sept. 2, 1974, Pub.L. 93-406, Title II, §§ 2001(g)(2)(C), 2002(g)(3), 2005(c)(5), 88 Stat. 957, 968, 991.

§ 902. Credit for corporate stockholder in foreign corporation

(a) Treatment of taxes paid by foreign corporation.—For purposes of this subpart, a domestic corporation which owns at least 10 percent of the voting stock of a foreign corporation from which it receives dividends in any taxable year shall—

(1) to the extent such dividends are paid by such foreign corporation out of accumulated profits (as defined in subsection (c)(1)(A)) of a year for which such foreign corporation is not a less developed country corporation, be deemed to have paid the same proportion of any income, war profits, or excess profits taxes paid or deemed to be paid by such foreign corporation to any foreign country or to any possession of the United States on or with respect to such accumulated profits, which the amount of such dividends (determined without regard to section 78) bears to the amount of such accumulated profits in excess of such income, war profits, and excess profits taxes (other than those deemed paid); and

(2) to the extent such dividends are paid by such foreign corporation out of accumulated profits (as defined in subsection (c)(1)(B)) of a year for which such foreign corporation is a less developed country corporation, be deemed to have paid the same proportion of any income, war profits, or excess profits taxes paid or deemed to be paid by such foreign corporation to any foreign country or to any possession of the

United States on or with respect to such accumulated profits, which the amount of such dividends bears to the amount of such accumulated profits.

(b) Foreign subsidiary of first and second foreign corporation.—

(1) If the foreign corporation described in subsection (a) (hereinafter in this subsection referred to as the "first foreign corporation") owns 10 percent or more of the voting stock of a second foreign corporation from which it receives dividends in any taxable year, it shall be deemed to have paid the same proportion of any income, war profits, or excess profits taxes paid or deemed to be paid by such second foreign corporation to any foreign country or to any possession of the United States on or with respect to the accumulated profits of the corporation from which such dividends were paid which—

(A) for purposes of applying subsection (a) (1), the amount of such dividends bears to the amount of the accumulated profits (as defined in subsection (c) (1) (A)) of such second foreign corporation from which such dividends were paid in excess of such income, war profits, and excess profits taxes, or

(B) for purposes of applying subsection (a) (2), the amount of such dividends bears to the amount of the accumulated profits (as defined in subsection (c) (1) (B)) of such second foreign corporation from which such dividends were paid.

(2) If such first foreign corporation owns 10 percent or more of the voting stock of a second foreign corporation which, in turn, owns 10 percent or more of the voting stock of a third foreign corporation from which the second foreign corporation receives dividends in any taxable year, the second foreign corporation shall be deemed to have paid the same proportion of

any income, war profits, or excess profits taxes paid by such third foreign corporation to any foreign country or to any possession of the United States on or with respect to the accumulated profits of the corporation from which such dividends were paid which—

(A) for purposes of applying subsection (a) (1), the amount of such dividends bears to the amount of the accumulated profits (as defined in subsection (c) (1) (A)) of such third foreign corporation from which such dividends were paid in excess of such income, war profits, and excess profits taxes, or

(B) for purposes of applying subsection (a) (2), the amount of such dividends bears to the amount of the accumulated profits (as defined in subsection (c) (1) (B)) of such third foreign corporation from which such dividends were paid.

(3) For purposes of this subpart, subsection (b) (1) shall not apply unless the percentage of voting stock owned by the domestic corporation in the first foreign corporation and the percentage of voting stock owned by the first foreign corporation in the second foreign corporation when multiplied together equal at least 5 percent, and for purposes of this subpart, subsection (b) (2) shall not apply unless the percentage arrived at for purposes of applying subsection (b) (1) when multiplied by the percentage of voting stock owned by the second foreign corporation in the third foreign corporation is equal to at least 5 percent.

(c) Applicable rules.—

(1) Accumulated profits defined.—For purposes of this section, the term "accumulated profits" means with respect to any foreign corporation—

(A) for purposes of subsections (a) (1), (b) (1) (A), and (b) (2) (A), the amount of its gains, profits,

or income computed without reduction by the amount of the income, war profits, and excess profits taxes imposed on or with respect to such profits or income by any foreign country or any possession of the United States; and

(B) for purposes of subsections (a) (2), (b) (1) (B), and (b) (2) (B), the amount of its gains, profits, or income in excess of the income, war profits, and excess profits taxes imposed on or with respect to such profits or income.

The Secretary or his delegate shall have full power to determine from the accumulated profits of what year or years such dividends were paid, treating dividends paid in the first 60 days of any year as having been paid from the accumulated profits of the preceding year or years (unless to his satisfaction shown otherwise), and in other respects treating dividends as having been paid from the most recently accumulated gains, profits, or earnings.

(2) Accounting periods.—In the case of a foreign corporation, the income, war profits, and excess profits taxes of which are determined on the basis of an accounting period of less than 1 year ,the word "year" as used in this subsection shall be construed to mean such accounting period.

(d) Less developed country corporation defined.—For purposes of this section, the term "less developed country corporation" means—

(1) a foreign corporation which, for its taxable year, is a less developed country corporation within the meaning of section 955(c)(1) or (2), and

(2) a foreign corporation which owns 10 percent or more of the total combined voting power of all classes of stock entitled to vote of a foreign corporation which

is a less developed country corporation within the meaning of section 955(c)(1), and—

(A) 80 percent or more of the gross income of which for its taxable year meets the requirement of section 955(c)(1)(A); and

(B) 80 percent or more in value of the assets of which on each day of such year consists of property described in section 955(c)(1)(B).

A foreign corporation which is a less developed country corporation for its first taxable year beginning after December 31, 1962, shall, for purposes of this section, be treated as having been a less developed country corporation for each of its taxable years beginning before January 1, 1963.

(e) Cross references.—

(1) For inclusion in gross income of an amount equal to taxes deemed paid under subsection (a)(1), see section 78.

(2) For application of subsections (a) and (b) with respect to taxes deemed paid in a prior taxable year by a United States shareholder with respect to a controlled foreign corporation, see section 960.

(3) For reduction of credit with respect to dividends paid out of accumulated profits for years for which certain information is not furnished, see section 6038.

Aug. 16, 1954, c. 736, 68A Stat. 286; Sept. 14, 1960, Pub.L. 86-780, § 6(b)(2), 74 Stat. 1016; Oct. 16, 1962, Pub.L. 87-834, § 9(a), 76 Stat. 999; Jan. 12, 1971, Pub.L. 91-684, §§ 1, 2, 84 Stat. 2068, 2069.

§ 903. Credit for taxes in lieu of income, etc., taxes

For purposes of this subpart and of sections 164(a) and 275(a), the term "income, war profits, and excess profits taxes" shall include a tax paid in lieu of a tax on income, war profits, or excess profits otherwise generally imposed by any foreign country or by any possession of the United States. Aug. 16, 1954, c. 736, 68A Stat. 287; Feb. 26, 1964, Pub.L. 88-272, Title II, § 207(b)(8), 78 Stat. 42.

§ 904. Limitation on credit

(a) Alternative limitations.—

(1) Per-country limitation.—In the case of any taxpayer who does not elect the limitation provided by paragraph (2), the amount of the credit in respect of the tax paid or accrued to any foreign country or possession of the United States shall not exceed the same proportion of the tax against which such credit is taken which the taxpayer's taxable income from sources within such country or possession (but not in excess of the taxpayer's entire taxable income) bears to his entire taxable income for the same taxable year.

(2) Overall limitation.—In the case of any taxpayer who elects the limitation provided by this paragraph, the total amount of the credit in respect of taxes paid or accrued to all foreign countries and possessions of the United States shall not exceed the same proportion of the tax against which such credit is taken which the taxpayer's taxable income from sources without the United States (but not in excess of the taxpayer's entire taxable income) bears to his entire taxable income for the same taxable year.

(b) Election of overall limitation.—

(1) In general.—A taxpayer may elect the limitation provided by subsection (a)(2) for any taxable year beginning after December 31, 1960. An election under

this paragraph for any taxable year shall remain in effect for all subsequent taxable years, except that it may be revoked (A) with the consent of the Secretary or his delegate with respect to any taxable year or (B) for the taxpayers' first taxable year beginning after December 31, 1969.

(2) Election after revocation.—Except in a case to which paragraph (1)(B) applies, if the taxpayer has made an election under paragraph (1) and such election has been revoked, such taxpayer shall not be eligible to make a new election under paragraph (1) for any taxable year, unless the Secretary or his delegate consents to such new election.

(3) Form and time of election and revocation.—An election under paragraph (1) and any revocation of such an election, may be made only in such manner as the Secretary or his delegate may by regulations prescribe. Such an election or revocation with respect to any taxable year may be made or changed at any time before the expiration of the period prescribed for making a claim for credit or refund of the tax imposed by this chapter for such taxable year.

(c) Taxable income for purpose of computing limitation. —for purposes of computing the applicable limitation under subsection (a), the taxable income in the case of an individual, estate, or trust shall be computed without any deduction for personal exemptions under section 151 or 642(b).

(d) Carryback and carryover of excess tax paid.—Any amount by which any such tax paid or accrued to any foreign country or possession of the United States for any taxable year beginning after December 31, 1957, for which the taxpayer chooses to have the benefits of this subpart exceeds the applicable limitation under subsection (a) shall be deemed tax paid or accrued to such foreign country or possession of the United States in the second preceding taxable year, in the first preceding taxable year, and in the first, second, third, fourth, or fifth succeeding taxable years, in that order and to the extent not deemed tax paid or accrued in a prior taxable year, in the amount by which the applicable limitation under subsection (a) for such preceding or succeeding taxable year exceeds the sum of the tax paid or accrued to such foreign country or possession for such preceding or succeeding taxable year and the amount of the tax for any taxable year earlier than the current taxable year which shall be deemed to have been paid or accrued in such preceding or subsequent taxable year (whether or not the taxpayer chooses to have the benefits of this subpart with respect to such earlier taxable year). Such amount deemed paid or accrued in any year may be availed of only as a tax credit and not as a deduction and only if taxpayer for such year chooses to have the benefits of this subpart as to taxes paid or accrued for that year to foreign countries or possessions. For purposes of this subsection, the terms "second preceding taxable year" and "first preceding taxable year" do not include any taxable year beginning before January 1, 1958.

(e) Carrybacks and carryovers where overall limitation is elected.—

(1) Foreign taxes to be aggregated for purposes of subsection (d).—With respect to each taxable year of the taxpayer to which the limitation provided by subsection (a)(2) applies, the taxes referred to in the first sentence of subsection (d) shall, for purposes of applying such first sentence, be aggregated on an overall basis (rather than taken into account on a per-country basis).

(2) Foreign taxes may not be carried from per-country year to overall year or from overall year to per-country year.—No amount paid or accrued for any taxable year to which the limitation provided by sub-

section (a)(1) applies shall (except for purposes of determining the number of taxable years which have elapsed) be deemed paid or accrued under subsection (d) in any taxable year to which the limitation provided by subsection (a)(2) applies. No amount paid or accrued for any taxable year to which the limitation provided by subsection (a)(2) applies shall (except for purposes of determining the number of taxable years which have elapsed) be deemed paid or accrued under subsection (d) in any taxable year to which the limitation provided by subsection (a)(1) applies.

(f) Application of section in case of certain interest income and dividends from a DISC or former DISC.—

(1) In general.—The provisions of subsections (a), (c), (d), and (e) of this section shall be applied separately with respect to each of the following items of income—

(A) the interest income described in paragraph (2),

(B) dividends from a DISC or former DISC (as defined in section 992(a)) to the extent such dividends are treated as income from sources without the United States, and

(C) income other than the interest income described in paragraph (2) and dividends described in subparagraph (B).

(2) Interest income to which applicable.—For purposes of this subsection, the interest income described in this paragraph is interest other than interest—

(A) derived from any transaction which is directly related to the active conduct of a trade or business in a foreign country or a possession of the United States,

(B) derived in the conduct of a banking, financing, or similar business,

(C) received from a corporation in which the taxpayer (or one or more includible corporations in an affiliated group, as defined in section 1504, of which the taxpayer is a member) owns, directly or indirectly, at least 10 percent of the voting stock,

(D) received on obligations acquired as a result of the disposition of a trade or business actively conducted by the taxpayer in a foreign country or possession of the United States or as a result of the disposition of stock or obligations of a corporation in which the taxpayer owned at least 10 percent of the voting stock.

For purposes of subparagraph (C), stock owned, directly or indirectly, by or for a foreign corporation shall be considered as being proportionately owned by its shareholders.

(3) Overall limitation not to apply.—The limitation provided by subsection (a)(2) shall not apply with respect to the interest income described in paragraph (2) or to dividends described in paragraph (1)(B). The Secretary or his delegate shall by regulations prescribe the manner of application of subsection (e) with respect to cases in which the limitation provided by subsection (a)(2) applies with respect to income described in paragraph (1)(B) and (C).

(4) Transitional rules for carrybacks and carryovers.—

(A) Carrybacks to years prior to Revenue Act of 1962.—Where, under the provisions of subsection (d), taxes (i) paid or accrued to any foreign country or possession of the United States in any taxable year beginning after the date of the enactment of the Revenue Act of 1962 are deemed (ii) paid or ac-

crued in one or more taxable years beginning on or before the date of enactment of the Revenue Act of 1962, the amount of such taxes deemed paid or accrued shall be determined without regard to the provisions of this subsection. To the extent the taxes paid or accrued to a foreign country or possession of the United States in any taxable year described in clause (i) are not, with the application of the preceding sentence, deemed paid or accrued in any taxable year described in clause (ii), such taxes shall, for purposes of applying subsection (d), be deemed paid or accrued in a taxable year beginning after the date of the enactment of the Revenue Act of 1962, with respect to interest income described in paragraph (2), and with respect to income other than interest income described in paragraph (2), in the same ratios as the amount of such taxes paid or accrued with respect to interest income described in paragraph (2), and the amount of such taxes paid or accrued with respect to income other than interest income described in paragraph (2), respectively, bear to the total amount of such taxes paid or accrued to such foreign country or possession of the United States.

(B) Carryover to years after Revenue Act of 1962.—Where, under the provisions of subsection (d), taxes (i) paid or accrued to any foreign country or possession of the United States in any taxable year beginning on or before the date of the enactment of the Revenue Act of 1962 are deemed (ii) paid or accrued in one or more taxable years beginning after the date of the enactment of the Revenue Act of 1962, the amount of such taxes deemed paid or accrued in any year described in clause (ii) shall, with respect to interest income described in paragraph (2) be an amount which bears the same ratio to the amount of such taxes deemed paid or accrued as the amount of

the taxes paid or accrued to such foreign country or possession for such year with respect to interest income described in paragraph (2) bears to the total amount of the taxes paid or accrued to such foreign country or possession for such year; and the amount of such taxes deemed paid or accrued in any year described in clause (ii) with respect to income other than interest income described in paragraph (2) shall be an amount which bears the same ratio to the amount of such taxes deemed paid or accrued for such year as the amount of taxes paid or accrued to such foreign country or possession for such year with respect to income other than interest income described in paragraph (2) bears to the total amount of the taxes paid or accrued to such foreign country or possession for such year.

(5) DISC dividends aggregated for purposes of per-country limitation.—In the case of a taxpayer who for the taxable year has dividends described in paragraph (1)(B) from more than one corporation, the limitation provided by subsection (a)(1) shall be applied with respect to the aggregate of such dividends.

(g) Cross reference.—

(1) For increase of applicable limitation under subsection (a) for taxes paid with respect to amounts received which were included in the gross income of the taxpayer for a prior taxable year as a United States shareholder with respect to a controlled foreign corporation, see section 960(b).

(2) For special rule relating to the application of the credit provided by section 901 in the case of affiliated groups which include Western Hemisphere trade corporations for years in which the limitation provided by subsection (a)(2) applies, see section 1503(b).

Aug. 16, 1954, c. 736, 68A Stat. 287; Sept. 2, 1958, Pub.L. 85-866, Title I, § 42(a), 72 Stat. 1639; Sept. 14, 1960, Pub. L. 86-780, § 1, 74 Stat. 1010; Oct. 16, 1962, Pub.L. 87-834, §§ 10(a), 12(b)(2), 76 Stat. 1002, 1031; Feb. 26, 1964, Pub. L. 88-272, Title II, § 234(b)(6), 78 Stat. 116; Nov. 13, 1966, Pub.L. 89-809, Title I, § 106(c)(1), 80 Stat. 1570; Dec. 30, 1969, Pub.L. 91-172, Title V, § 506(b), 83 Stat. 635; Dec. 10, 1971, Pub.L. 92-178, Title V, § 502(b)(2)-(4), 85 Stat. 549.

§ 905. Applicable rules

(a) Year in which credit taken.—The credits provided in this subpart may, at the option of the taxpayer and irrespective of the method of accounting employed in keeping his books, be taken in the year in which the taxes of the foreign country or the possession of the United States accrued, subject, however, to the conditions prescribed in subsection (c). If the taxpayer elects to take such credits in the year in which the taxes of the foreign country or the possession of the United States accrued, the credits for all subsequent years shall be taken on the same basis, and no portion of any such taxes shall be allowed as a deduction in the same or any succeeding year.

(b) Proof of credits.—The credits provided in this subpart shall be allowed only if the taxpayer establishes to the satisfaction of the Secretary or his delegate—

(1) the total amount of income derived from sources without the United States, determined as provided in part I,

(2) the amount of income derived from each country, the tax paid or accrued to which is claimed as a credit under this subpart, such amount to be determined under regulations prescribed by the Secretary or his delegate, and

(3) all other information necessary for the verification and computation of such credits.

For purposes of this subpart, the recipient of a royalty or other amount paid or accrued as consideration for the use of, or for the privilege of using, copyrights, patents, designs, secret processes and formulas, trademarks, and other like property, and derived from sources within the United Kingdom of Great Britain and Northern Ireland, shall be deemed to have paid or accrued any income, war-profits and excess-profits taxes paid or accrued to the United Kingdom with respect to such royalty or other amount (including the amount by which the payor's United Kingdom tax was increased by inability to deduct such royalty or other amount) if such recipient elects to include in its gross income the amount of such United Kingdom tax.

(c) Adjustments on payment of accrued taxes.—If accrued taxes when paid differ from the amounts claimed as credits by the taxpayer, or if any tax paid is refunded in whole or in part, the taxpayer shall notify the Secretary or his delegate, who shall redetermine the amount of the tax for the year or years affected. The amount of tax due on such redetermination, if any, shall be paid by the taxpayer on notice and demand by the Secretary or his delegate, or the amount of tax overpaid, if any, shall be credited or refunded to the taxpayer in accordance with subchapter B of chapter 66 (sec. 6511 and following). In the case of such a tax accrued but not paid, the Secretary or his delegate, as a condition precedent to the allowance of this credit, may require the taxpayer to give a bond, with sureties satisfactory to and to be approved by the Secretary or his delegate, in such sum as the Secretary or his delegate may require, conditioned on the payment by the taxpayer of any amount of tax found due on any such redetermination; and the bond herein prescribed shall contain such further conditions as the Secretary or his delegate may require. In such redetermination by the Secretary or his delegate of the amount of tax due from the taxpayer for the year or years affected by a refund, the amount of the taxes refunded for which credit has been allowed

under this section shall be reduced by the amount of any tax described in section 901 imposed by the foreign country or possession of the United States with respect to such refund; but no credit under this subpart, and no deduction under section 164 (relating to deduction for taxes) shall be allowed for any taxable year with respect to such tax imposed on the refund. No interest shall be assessed or collected on any amount of tax due on any redetermination by the Secretary or his delegate, resulting from a refund to the taxpayer, for any period before the receipt of such refund, except to the extent interest was paid by the foreign country or possession of the United States on such refund for such period. Aug. 16, 1954, c. 736, 68A Stat. 288; Sept. 2, 1958, Pub.L. 85-866, Title I, § 103(b), 72 Stat. 1675.

APPENDIX F
Statement D of Stall Exhibit No. 1

CABOT CORPORATION

COMPUTATION OF FEDERAL INCOME TAX LIABILITY USED IN COMPUTING COST OF SERVICE

FOR THE TWELVE MONTHS ENDED SEPTEMBER 30, 1972

Line No.		Source Statement	Total	Division		Allocation of Division 00 to Functional Operations			
				00	75	Natural Gas Production	Underground Storage	Transmission	Distribution
		(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
			$	$	$	$	$	$	$
1	Average Rate Base	B	11,506,917	11,262,393	244,524	4,821,966	1,781,262	2,695,039	1,964,126
2	Return at 8.5 Percent	B	978,088	957,303	20,785	409,867	151,407	229,078	166,951
3	Adjustments for Tax Purposes:	A							
4	Additions:								
5	Utility Depreciation		571,481	566,720	4,761	347,853	25,545	110,057	83,265
6	Depreciation to Clearing Accounts		41,430	41,430		12,075	1,045	14,380	13,930
7	Total Additions		612,911	608,150	4,761	359,928	26,590	124,437	97,195
8	Deductions:								
9	Interest on Meter Deposits		5,927	5,927					5,927
10	Interest on Long-Term Debt (Pro-rata)		333,438	325,419	8,019	139,328	51,468	77,871	56,752
11	Federal Tax Depreciation		594,980	591,340	3,640	349,979	25,855	120,997	94,509
12	Federal Tax Depletion		302,840	299,520	3,320	299,520			
13	Total Deductions		1,237,185	1,222,206	14,979	788,827	77,323	198,868	157,188
14	Net Tax Adjustments		(624,274)	(614,056)	(10,218)	(428,899)	(50,733)	(74,431)	(50,993)
15	Balance of Return After Tax		353,814	343,247	10,567	(19,032)	100,674	154,647	106,958
16	Amount of Income Subject to Tax Line 15 : (100% — 48% × 74.718% Savings From Consolidation) or 87.8640%		402,681	390,654	12,027	(21,661)	114,579	170,000	121,730
17	Federal Income Tax at 48%		193,287	187,514	5,773	(10,397)	54,998	84,483	58,430
	Less: Consolidated Savings at 74.718%		(144,420)	(140,107)	(4,313)	7,768	(41,093)	(63,124)	(43,658)
18	Net Amount of Tax		48,867	47,407	1,400	(2,629)	13,905	21,359	14,772

IN THE

Supreme Court of the United States

October Term, 1975

No. 75-602

CABOT CORPORATION,

Appellant,

v.

THE PUBLIC SERVICE COMMISSION OF WEST VIRGINIA,

Appellee.

ON APPEAL FROM THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

MOTION TO DISMISS OR AFFIRM

THOMAS N. HANNA
Attorney for Appellee
E-206 State Capitol Building
Charleston, West Virginia 25305

December 10, 1975

JARRETT PRINTING COMPANY, CHARLESTON, W. VA.

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MOTION TO DISMISS OR AFFIRM

Appellee, The Public Service Commission of West Virginia, pursuant to Rule 16 of the Rules of the Supreme Court of the United States, moves the Court to dismiss the appeal herein or in the alternative to affirm the judgment of the Supreme Court of Appeals of West Virginia, on the ground that it is manifest that the questions on which the decision of the cause depends are so unsubstantial as not to need further argument.

I. THE COMMISSION ORDER INVOLVED AND THE NATURE OF THE CASE.

The Appellant, Cabot Corporation (hereinafter "Cabot"), is a multi-national corporation which alone, or through its subsidiaries, has plants and operations in the United States and in more than ten foreign countries, with total sales for the fiscal year 1974 of slightly over $400,000,000. Rather than organize a subsidiary corporation Cabot has established a Gas Marketing Division which operates in West Virginia an intrastate natural gas utility serving some 22,000 residential, commercial and small industrial customers in nine West Virginia counties. This Gas Marketing Division also includes two corporate subsidiaries, Industrial Gas Corporation and Mountain Gas Company, both of which are interstate gas pipeline companies. West Virginia is the only State in which Cabot operates a gas distribution utility and it is the third largest such utility in the State.

On February 1, 1973, Cabot filed with the Public Service Commission of West Virginia (hereinafter "Commission"), pursuant to Chapter 24, Article 2, Section 4 of the West Virginia Code, 1931, as amended[1] (hereinafter "Code"), revised tariff sheets stating an increase of approximately 19% in rates and charges for furnishing gas service to customers throughout West Virginia, to become effective March 19, 1973. Assigning the matter Case No. 7612, the Commission, pursuant to Code 24-2-4, suspended the effective date of the revised tariff sheets until July 6, 1973, when they became effective subject to refund under a $550,000 bond, and initiated an investigation into the reasonableness of the proposed rates and charges.

[1]Reprinted in Appellant's "Appendix to Jurisdictional Statement" (hereinafter "Appendix") at pp 15a-17a.

Evidentiary hearings were held before the Commission on December 11, 1974, and January 24, 1975, at the close of which the matter was submitted for decision, subject to the filing of briefs. The last brief, Intervenor True Temper Corporation's reply brief, was filed March 31, 1975.

On June 13, 1975, the Commission entered an order[2] which granted Cabot an increase of $433,961. On July 11, 1975, Cabot filed its Petition for Suspension and Appeal of the aforesaid order with the West Virginia Supreme Court of Appeals, which, after oral argument on July 22, 1975, denied said petition by order entered July 23, 1975.[3] Cabot's appeal to this Court followed.

ARGUMENT

II. THE COMMISSION ORDER OF JUNE 13, 1975, DID NOT DEPRIVE CABOT OF ITS PROPERTY WITHOUT JUST COMPENSATION AND THIS CASE DOES NOT PROVIDE A SUBSTANTIAL FEDERAL QUESTION.

The Appellant alleges in this Appeal that the Commission's order of June 13, 1975, fixing the maximum rates and charges which Appellant's intrastate gas utility operation may charge its customers violates the Fourteenth Amendment. The specific issue is the Commission's calculation of the Appellant's Federal Income Tax liability to be assigned for rate making purposes to its West Virginia utility operation. In the aforesaid order the Commission adopted the staff's method of calculating an effective rate of 12.13536% to be applied to Appellant's taxable income in its West Virginia utility oper-

[2]Appendix at pp 3a-12a.
[3]Appendix at pp 1a-2a.

ation of $417,690 producing a tax liability of $50,688. In calculating this effective rate, the staff started with the amount of income taxes actually paid to the Federal Government, an amount reduced by the use of foreign tax credits, and figured the tax saving resulting to the Appellant. This tax saving was then multiplied by the statutory rate of 48% and the product was subtracted from the statutory rate in arriving at the effective rate of 12.13536%. The Appellant argues in this case that the use of anything less than the statutory rate of 48% applied to its West Virginia utility's taxable income is confiscatory.

The Commission believes there is ample authority and precedent for a regulatory Commission to reduce a company's tax allowance in its cost of service to the point where the effective rate is less than the statutory rate in cases where consolidated returns are filed or where the actual tax paid the Federal Government is reduced through the use of various tax credits. In the case of consolidated returns, it was held that the Federal Power Commission acted properly in recognizing savings resulting from an election by affiliated companies to file consolidated income tax returns and limiting the expenses allowed in the cost of service to real expenses. *Federal Power Commission* v. *United Gas Pipe Line Company*, 386 US 237 (1967).

Finally, we submit that it is not the action of this Commission, but the failure of Cabot to set up a separate subsidiary corporation for its West Virginia utility operation and to have that utility file a separate Federal Tax return that has resulted in Cabot not being allowed a tax rate in its cost of service at the full statutory rate of 48%.

CONCLUSION

For all the above reasons, Appellee, The Public Service Commission of West Virginia, respectfully submits that the questions upon which this cause depend are so unsubstantial as not to need further argument, and Appellee respectfully moves the Court to dismiss this Appeal or, in the alternative, to affirm the judgment entered in the cause by the Supreme Court of Appeals of West Virginia.

Respectfully submitted,

THOMAS N. HANNA
Attorney for Appellee
E-206 State Capitol Building
Charleston, West Virginia 25305

December 10, 1975

IN THE

Supreme Court of the United States

OCTOBER TERM, 1975

No. 75-602

CABOT CORPORATION, *Appellant,*

v.

PUBLIC SERVICE COMMISSION OF WEST VIRGINIA and TRUE TEMPER CORPORATION, *Appellees.*

On Appeal from the West Virginia Supreme Court of Appeals

APPELLANT'S REPLY MEMORANDUM TO MOTION TO DISMISS OR AFFIRM

F. PAUL CHAMBERS
MICHAEL A. ALBERT
1601 Kanawha Valley Building
Charleston, West Virginia 25301

WALTER F. GREELEY
EDWIN S. NAIL
Cabot Corporation
125 High Street
Boston, Massachusetts 02110

Attorneys for Appellant

Of Counsel:

WILLIAM G. CHARLTON
Cabot Corporation
Charleston National Plaza
Charleston, West Virginia 25302

PRESS OF BYRON S. ADAMS PRINTING, INC., WASHINGTON, D. C.

IN THE

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PUBLIC SERVICE COMMISSION OF WEST VIRGINIA and TRUE TEMPER CORPORATION, *Appellees.*

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APPELLANT'S REPLY MEMORANDUM TO MOTION TO DISMISS OR AFFIRM

The Appellee, Public Service Commission ("Commission"), in its motion to dismiss or affirm in this case, cited only *Federal Power Commission* v. *United Gas Pipe Line Company,* 386 U.S. 237 (1967), as "authority and precedent for a regulatory Commission to reduce a company's tax allowance in its cost of service to the point where the effective rate is less than the statutory rate in cases where consolidated returns are filed or

where the actual tax paid the Federal Government is reduced through the use of various tax credits.'' Appellees Motion at 4 (emphasis added).

This Court in *United Gas Pipe Line Company* did not establish "precedent and authority" for, or in anyway concern itself with, the above italicized proposition. Instead, *United Gas Pipe Line Company* stated only that the FPC "could properly disallow the *hypothetical tax expense* [based on the amount payable if all the companies within the affiliated group had filed a separate federal income tax return] and hold that rates based on such an unreal cost of service would not be just and reasonable." That is not the issue in Cabot Corporation's ("Cabot's") appeal.

Appellant considered and rejected citation to *United Gas Pipe Line Company, supra,* because it is not relevant to the legislation (the Commission's order) here complained of.

As to the vacuous contention made by the Commission in its motion to dismiss that Cabot should have set up a subsidiary corporation for its West Virginia utility operations to file a separate federal tax return, this theory was not considered by the Commission and is raised for the first time in this Court. There is no way under existing federal tax law that an affiliated group filing a consolidated return can break out one affiliate for purposes of that affiliate filing a separate return. 26 U.S.C. § 1501; Treas. Reg. § 1.1502-75 (1966); Rev. Rul. 56-559, 1956-2 Cum. Bul. 595.

For the foregoing reasons and those set forth in Cabot's Jurisdictional Statement filed with this Court in this matter, the need for full plenary consideration

of this appeal and for reversal of the Commission's order is indisputable.

Respectfully submitted,

F. PAUL CHAMBERS
MICHAEL A. ALBERT
1601 Kanawha Valley Building
Charleston, West Virginia 25301

WALTER F. GREELEY
EDWIN S. NAIL
Cabot Corporation
125 High Street
Boston, Massachusetts 02110

Attorneys for Appellant

Of Counsel:
WILLIAM G. CHARLTON
Cabot Corporation
Charleston National Plaza
Charleston, West Virginia 25302

December 15, 1975